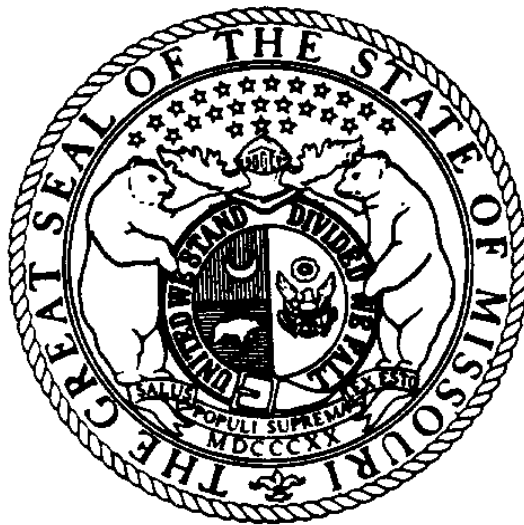


**REPORT
OF
SENATE INTERIM COMMITTEE
ON
TITLE INSURANCE**



January 2006

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COMMITTEE ON TITLE INSURANCE

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Prepared by

Stephen Witte, Senate Research Staff Attorney

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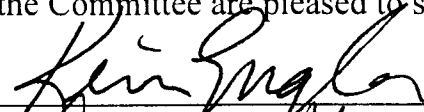
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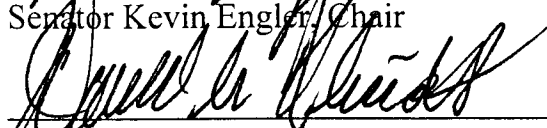
The Honorable Michael Gibbons, President Pro Tem of the Senate
State Capitol
Jefferson City, MO 65101

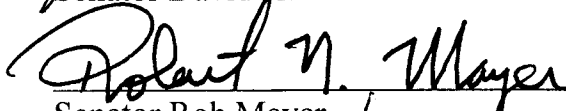
Dear Mr. President:

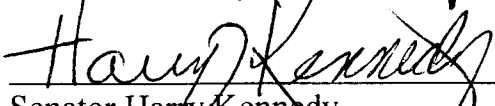
Pursuant to your charge and the provisions of Senate Rule 31, the Senate Interim Committee on Title Insurance gathered information from a variety of sources during the summer months of 2005. The committee heard testimony from title insurance company representatives, real estate company representatives, home builder representatives, employees from the Missouri Department of Insurance and private citizens. Due to recent closings of title agencies in the St. Louis area, title insurance agent defalcations, and other problems experienced by home buyers, home builders and other members of the title insurance industry, the Senate Interim Committee on Title Insurance explored various reform measures to stabilize, strengthen, and professionalize the title insurance market.


There is widespread interest in reforming Missouri's title insurance laws in order to protect Missouri home buyers. The committee expresses its gratitude to all the parties who provided vital information and assistance on this issue. The undersigned members of the Committee are pleased to submit the attached report.



Senator Kevin Engler, Chair

Senator David Klindt

Senator Rob Mayer

Senator Harry Kennedy

Senator Frank Barnitz

Senate Interim Committee on Title Insurance

I. OVERVIEW

In the wake of several title insurance agencies closing their doors in the St. Louis area, the Senate Interim Committee on Title Insurance was created on June 27, 2005. The committee was charged primarily with studying the state laws and regulations relating to the title insurance industry. The joint interim committee additionally was charged with:

- 1) Examining industry issues that are currently affecting Missouri consumers;
- 2) Exploring and clarifying the duties and responsibilities of title insurance agents;
- 3) Reviewing the protection and enforcement of consumer and lender funds; and
- 4) Examining the process of setting title insurance rates.

The Committee held a number of public hearings and solicited testimony regarding a wide range of concerns related to title insurance. Hearings were held in the following locations:

August 19, 2005	Des Peres, MO
September 1, 2005	Farmington, MO
September 14, 2005	Jefferson City, MO

Based on the testimony and handouts provided by title insurance companies, title insurance agents, home builders, realtors, banks, and home buyers, the interim committee developed and adopted a list of recommendations. What follows is a summary of the testimony received by the committee in section II of this report and the recommendations that have been adopted by the committee in section III of this report.

II. SUMMARY OF TESTIMONY

In the course of three public hearings, the committee gathered a tremendous amount of information about the many issues facing the title insurance industry. What follows is a summary of the testimony heard by the committee regarding those issues.

A. Des Peres, Missouri Meeting

On August 19, 2005, the interim committee held its first meeting in Des Peres, Missouri. A variety of groups testified before the committee regarding the current status of the title insurance industry.

Herb Lessler, of MLS Homes, testified on behalf of the Home Builders Association of Greater St.

Louis. He stated that the Home Builders Association of Greater St. Louis is against any rate setting mechanism. Rate setting would guarantee higher profits for the insurance companies at the expense of the consumer. Mr. Lessler stated that if a rate setting mechanism from a 2000 bill (SB 894) would have been found constitutional, consumers would be paying 64% more for title insurance. Mr. Lessler noted that Missouri is a low cost title insurance state. For example, title insurance in Florida is \$5.75 per thousand, while Missouri is \$3.50 per thousand (a difference of 64%). He stated that raising title insurance rates would make it more difficult for some Missourians to purchase homes (for every \$1,000 increase in housing costs, an additional 300,000 families are unable to buy a home). Mr. Lessler stated that he was supportive of other title insurance reforms found in the 2000 bill and believed such reforms would alleviate many of the current problems faced by the title insurance industry.

Carole McCabe, the Regional Vice President of Caldwell Banker Gundaker Realtors, testified in favor of implementing a stable rate system. She stated that cut-throat rate competition in the St. Louis area has led to some companies shutting their doors since they could not cover their outstanding claims. In addition to implementing a stable rate system, she spoke in favor of educational requirements for title agents and regular auditing of title agency accounts.

Sam Licklider testified on behalf of Missouri Association of Realtors. He raised six points with the committee. First, he stated that the realtors are wary of fixed title insurance rates statewide unless it can be proved it will stabilize the industry. He stated that if the committee felt it necessary to establish a rate-setting mechanism, then there should be some type of system of oversight, perhaps modeled on the Public Service Commission, or a judicial proceeding. Second, Mr. Licklider testified that his association has reservations about requiring electronic transfer of funds because he believed a new federal law known as "Check 21" will solve most of the fund transmittal problems. Third, Mr. Licklider testified that his association does not want the state to mandate the issuance of guaranteed closing letters because it would increase costs to the home buying public without much benefit. Fourth, Mr. Licklider testified that the committee should explore the issue of liens as they pertain to title insurance. Fifth, Mr. Licklider stated that he would like to see that periodic audits are conducted of the escrow accounts of the title agents (by the underwriter, state or both). Finally, Mr. Licklider noted that the state should prohibit title agents from commingling funds (mandated escrow accounts).

Nancy LoRusso, the President of U.S. Title, noted that Missouri title agents and underwriters have been advocating title insurance law reform for several years. She noted that it has taken a rash of major defalcations to bring the issue back to the forefront. Mrs. LoRusso suggested that the committee consider the following recommendations:

- 1) Increase the competency and professionalism of title agents by mandating education requirements for title agents;
- 2) Toughen the requirements for auditing of agents by underwriters and improve the underwriters' ability to audit. The state should require annual audit of agencies and underwriters should be allowed to jointly audit agencies with multiple affiliations;

- 3) Clarify and strengthen the Department of Insurance's ability to inspect and audit agency books when necessary;
- 4) Require title insurance underwriters to notify the department of insurance of agent terminations;
- 5) Redefine the term "premium" to reflect the price actually paid by the consumer;
- 6) Require mandatory disclosure of title commitments;
- 7) Examine the issue of incentives offered by affiliated companies.
- 8) Toughen the "good funds" law to assure that there is money in the bank to back commitments made at closings;
- 9) Mandate closing protection letters which provide protection for funds of lenders, home buyers and home sellers;
- 10) Prohibit commingling of escrow funds with other title agency funds and assure that all escrow funds are in segregated accounts that can only be assessed via written instructions;
- 11) Establish deadlines for policy issuance;
- 12) Toughen mechanic lien laws so that contractors cannot dump their debts upon title insurance companies;
- 13) Establish a new procedure for setting title insurance rates to assure fair price and solvency; and
- 14) Prohibit split closings (split escrows).

Mike Starrett, the First Vice President of Missouri Land Title Association testified on behalf of the association. Mr. Starrett primarily addressed the issue of rate setting. Noting that title insurance is a risk based product and not a market based product, Mr. Starrett stated that the bidding war practices occurring in the St. Louis region has led to title insurance insolvencies. He stated that rates should be determined by adequate regulation by the department of insurance and not just free market conditions. He noted, however, that the current law is inadequate to ensure this result. Mr. Starrett testified that the problem with the current title insurance law is that the statutory definition of premium rate does not include a definition of "risk rate". He noted that Kansas and Nebraska require the filing of an "all inclusive rate" which includes the search and exam component so the rate is actually what the consumer is charged for the title insurance policy. He stated that Missouri's risk rate should bear a relationship to what is actually charged to the consumer and therefore needs to include search and examination fees.

Mr. Starrett also recommended that Missouri title insurance underwriters should file rates through the use of a rating bureau. Mr. Starrett also mentioned that in some states such as Texas, New Mexico and Florida, the state gathers data and promulgates the rates to be charged. In New Mexico, underwriters and agents provide the state audited financial statements and other statistical data. With that information, the department establishes a rate. Arizona also requires underwriters and agents to send in financial statements so the department can set rates.

Walter Whisler, the Senior Vice President of Stewart Title Guaranty Company, described the role of a title insurance underwriter and a title agent in a real estate transaction. Mr. Whisler provided data which showed that Missouri had the third highest loss ratio in 2004. Missouri's loss ratio is 12.2%, approximately 3 times the national average of 4.07%. Loss ratio is the amount of premium revenue paid back in claims. Mr. Whisler stated that Missouri's loss ratio is a combination of large claim payouts and low premiums. To address the inadequate premium problem, Mr. Whisler would support a ratings bureau in which all underwriters would submit their premium and loss data. Mr. Whisler stated that he would also like to see the legislature address the issues of mechanic liens and mortgage fraud.

Alan Sheehy, a private citizen, testified that he lost approximately \$80,000 when Capital Title Insurance Company shut down in January of 2005. Mr. Sheehy stated that he lost his money when Capital Title commingled Mr. Sheehy's closing funds with the company's operating funds.

Stewart Schneider, an underwriting attorney for First American Title Insurance Company, discussed how his company has resolved home buyer claims when two title insurance companies (Capital Title and Title Insurers) were placed into receivership. Mr. Schneider testified his company has had to pay out \$10.5 million in claims due to the insolvency of Capital Title Insurance. Mr. Schneider also shared some actual tragedies experienced by home buyers whose moneys were lost due to the insolvencies.

Celeste Rueter, a realtor with Coldwell Banker Gundaker of St. Louis, discussed a specific case where her clients lost large sums of monies after Title Insurers closed up in June 2005.

Kevin Overstreet, testified on behalf of Freedom Title Company. Mr. Overstreet suggested that there should be some type of rate promulgation procedure or regulation concerning title fees. He also suggested that the state should regulate affiliated business arrangements. Mr. Overstreet stated that the state should constrain affiliated business arrangements by requiring a minimum percentage of a title company's business must come from sources outside the parent company. For example, Kansas requires that at least 30% of a title company's business must be from outside sources. Mr. Overstreet also suggested that Missouri should end the practice of split closings. In Illinois, both sides of the transaction must close with the same title company.

Mark Sandau, testified on behalf of Mortgage Bankers Association of Missouri. It was his observation that most of the problems with the title insurance industry are occurring in the St. Louis area. Although Mr. Sandau testified against prohibiting split closings and rate promulgation in general, he did suggest the following title insurance reforms:

- 1) Independently audit the title agent accounts (operating accounts, escrow accounts, construction disbursement accounts and any other custodial accounts). There should be an absolute prohibition to commingling of accounts;
- 2) Require closing protection letters that protect all parties, including the seller;
- 3) Establish capital reserve requirements for title agencies, but not so stringent as to penalize rural title agencies; and
- 4) Establish time limits for the issuance of title policies. Mr. Sandau would like to see title insurance companies deliver their policies within 30 days after the closing.

B. Farmington Meeting

On September 1, 2005, the committee met in Farmington, Missouri. The committee heard testimony from several people who had testified at the committee's prior meeting. The focus of the hearing was to determine whether the title insurance problems plaguing the St. Louis area were also plaguing out-state Missouri.

The committee heard from Cara Detring, the principal owner of Preferred Land Title Company. She testified that the title insurance problems occurring in the St. Louis region are also occurring in out-state Missouri. Although defalcations have not taken place in out-state Missouri, many of the conditions that have precipitated defalcations and insolvencies in the St. Louis region, such as low-ball rate quotes, exist in out-state Missouri. Mrs. Detring testified that Missouri's reputation among the title insurance industry is poor. Mrs. Detring also stated that title agents are not perceived as professionals since Missouri does not require licensed title insurance agents to undergo education, testing or continuing education programs. Mrs. Detring further testified that there is little enforcement of the current title insurance regulations because the Department of Insurance does not have the funds to support additional manpower.

Mrs. Detring stated that out-state title insurance agencies are also experiencing problems with good funds. She stated that title insurance agencies spend an inordinate amount of time chasing down funds or delaying transactions because funds are not available to disburse during a closing. Mrs. Detring also stated that title insurance agencies are experiencing problems with split

closings. Finally, Mrs. Detring addressed the issue of affiliated business arrangements. She noted that such arrangements are not prevalent in out-state Missouri. Most affiliated business arrangements in out-state Missouri are RESPA compliant according to Mr Detring.

James Barrett, the Executive Vice President of First Service Bank, testified that the Department of Insurance does not have funds available to adequately regulate the title insurance industry. He suggested that title insurance companies should pay a small fee for each title insurance policy issued within the state to pay for increased enforcement. He noted that Illinois requires title insurance companies to pay \$3 for each policy issued. As for other title insurance reforms, Mr. Barrett suggested that the legislature:

- 1) Reform the state's mechanic lien laws;
- 2) Prohibit the commingling of escrow accounts;
- 3) Require closing protection letters that protect all parties involved in the transaction; and
- 4) Require wired funds as good funds.

Glenna Ard, a real estate broker and manager for Coldwell Banker, discussed how Missouri and Illinois are different with respect to certain practices in the title insurance industry. She stated that in Illinois, the seller pays for title insurance and therefore picks the title agency and closer. Furthermore, Illinois does not allow split closings. Mrs. Ard also mentioned that Southern Illinois has a stable rate structure compared to the St. Louis region.

Nancy LoRusso, President of U.S. Title, distributed handouts to the committee members, including copies of the Model Title Insurers Act and the Model Title Insurance Agent Act from the National Association of Insurance Commissioners (NAIC). Mrs. LoRusso also distributed a handout which compares key provisions of Missouri law, the NAIC model acts and Utah's title insurance law. Mrs. LoRusso testified that the model acts could serve as a general guideline for reforming Missouri's title insurance law.

Mike Starrett testified on behalf of Land America regarding closing protection letters. Mr. Starrett testified that closing protection letters should be required to protect parties during a closing. He stated that closing protection letters insure a buyer and a lender against title agent misappropriation. There is no charge for this protection since the buyer and lender are already insured. The seller, however, is not afforded protection under a closing protection letter. Mr. Starrett believes closing protection letters need to provide protection to the seller as is the case in Nebraska. Mr. Starrett also reiterated Cara Detring's comments that the Department of Insurance does not have the personnel or funds to adequately monitor the title insurance industry. He stated that the industry should provide funds to the Department of Insurance by imposing a small surcharge on the number of title insurance policies issued in the state. He noted that Illinois charges \$3 per policy issued. Missouri title agents issue approximately 350,000 title insurance

policies a year.

Pam Hart testified on behalf of the Missouri Land Title Association. She provided a survey of title insurance rates from across Missouri. The survey demonstrated that title insurance rates are being discounted statewide. Nineteen title companies reported that they were forced to offer discounted rates in order to retain the transaction.

Mark Sandau testified on behalf of Mortgage Bankers Association. Mr. Sandau restated the title insurance reforms he mentioned at the Des Peres meeting.

Sarah Jennings, a former processor for Phoenix Title Insurance, testified to the committee that she had lost \$500 in earnest money because of the closing of Phoenix Title. She also lost her job with the company. Ms. Jennings has experienced problems with collecting on her paychecks from Phoenix Title and has not been able to get back her earnest money. Ms. Jennings stated that the problems with Phoenix Title were wire fraud and commingling of accounts.

Robert McFessel, the Regional Vice President of First American Title Insurance Company, testified that since an average title insurance agency moves \$17 million through their accounts every month, any attempts to audit the accounts might prove to be difficult.

Mike Poppe, the Regional Audit Manager of First American Title Insurance Company, testified that defalcations are occurring in other states. He stated that many of the defalcations are due to companies trying to grow too quickly causing their operating accounts to dwindle. To recover operating funds, some title agencies offer discounted rates to attract business. The rates, however, are often lower than the actual cost to issue the title insurance.

C. JEFFERSON CITY HEARING

The interim committee met in Jefferson City on September 14, 2005. The committee heard testimony from a variety of interested parties, including the Director of the Department of Insurance.

Mark Abel, a consultant for U.S. Title, presented a video to the committee which narrated the accounts of different consumers who had been affected by recent title insurance defalcations and insolvencies.

Craig Olschansky, a real estate attorney for Thompson Coburn, testified on behalf of the Home Builders Association of Greater St. Louis. Mr. Olschansky characterized the current economic status of the title insurance industry as booming despite the fact that several title companies have exited the market in the St. Louis region. Mr. Olschansky testified that title insurance losses typically result from defalcations, errors in the underwriting process and unrecorded and

undiscoverable matters. He stated that the defalcation issue could be addressed by imposing stricter licensing, auditing and bonding requirements on title insurance agents. With respect to the unrecorded matters, Mr. Olschansky stated that since Missouri's mechanic lien law allows subcontractors to file a lien after the closing has occurred, title insurers are unable to properly account for their risk. The Home Builders Association is opposed to requiring builders to post bonds or establish escrow accounts, but would not oppose stricter false affidavit laws. The Home Builders Association is opposed to rate setting mechanisms in that states that promulgate rates generally have higher title insurance rates. The Home Builders Association is concerned that higher title insurance rates will affect the ability of people to purchase homes. The Home Builders Association is in favor of curbing illegal kickbacks and other arrangements that hinder open competition.

Joe Reis, the Senior Vice President of NRT Incorporated testified that it is too easy for a person to establish a title insurance agency in Missouri. In addition to supporting additional oversight by the Department of Insurance over the industry, Mr. Reis stated that Missouri needs stable and fair rates which will protect the home buyer and lender in the long run.

J. Scott McCall testified on behalf of LandAmerica Financial Group. Mr. McCall first addressed the issue of title insurance rates. He stated that the goal of any title insurance reform legislation should include a rate setting mechanism which would stabilize the rates in Missouri. Mr. McCall discussed the various methods used by other states to establish rates. Mr. McCall also discussed the importance of closing protection letters. Since title insurance does not protect the buyer or lender against escrow fraud or theft of funds at closing, closing protection letters are needed to provide this type of coverage. A nominal fee should be charged for such protection.

Joe Crutchfield testified on behalf of Investors Title Company of St. Louis. According to Mr. Crutchfield, the key component of any title insurance reform legislation is rate stabilization. Mr. Crutchfield stated that if the 2000 bill would not have been held unconstitutional, the current problems that plague the industry would not exist. Mr. Crutchfield also spoke in favor of audits and modifying Missouri's good funds law.

Mike Holden testified on behalf of Guaranty Land Title. Mr. Holden spoke in favor of adopting a Kansas statute which prohibits the commingling of funds, requires periodic auditing of such accounts, and requires the use of collected or good funds at closings. Mr. Holden also reiterated the need for rate stabilization in Missouri noting that the use of an all-inclusive rate would help reach that goal. Mr. Holden also noted that mechanic liens were a problem in Missouri. He recommended that Missouri adopt a Florida law which requires owners to file a notice of commencement of construction prior to the improvement of any property (Chapter 713). The Florida law adopts a notice recording device, under which the owner, prior to the beginning of work on an improvement, records a "notice of commencement" which puts third parties on notice that construction liens may be claimed against the real estate. If a lien claimant records his lien

during the effective period of a notice of commencement, his priority date is the date the notice of commencement was recorded. Mr. Holden also recommended prohibiting the practice of split closings.

Mike Starrett, the First Vice President of Missouri Land Title Association also spoke in favor of reforming Missouri's mechanic lien laws. He stated that often it is impossible to discover liens that are filed after closing since Missouri law allows contractors to file liens 60 days after the commencement of work. He would like for Missouri to adopt a law that would require liens to be filed before a home is sold. He mentioned the Nebraska Construction Lien Act.

Nancy LoRusso, the president of U.S. Title, testified that any title insurance reform legislation considered by the Missouri General Assembly must include some type of reform of title insurance rates.

Sam Licklider, a lobbyist for the Missouri Association of Realtors, testified that his association would be against prohibiting split closings. He stated that his association would not be opposed to imposing a small fee to allow the Department of Insurance to conduct audits of the title industry so long as the fee is imposed upon the issuance of a policy and not the recording of a title. Finally, Mr. Licklider stated that he would not be opposed to closing protection letters that protected all parties so long as the fee is reasonable.

Dale Finke, the Director of the Department of Insurance, addressed the committee with some possible reforms the Department of Insurance would like the General Assembly to implement. Some of the reforms mentioned by Mr. Finke included annual audits of escrow accounts, licensing and education requirements for title agents, issuance of closing protection letters and redefining Missouri's definition of premium. Mr. Finke stated that he would present the committee with a formal list of the department's recommendations at a later date.

III. RECOMMENDATIONS

After review of all information received by the committee during its three public hearings, the committee determined that the following recommendations should be made to the General Assembly. The committee recommends that it should be the policy of Missouri to:

1. Require active oversight and regular auditing of all title agency accounts (escrow, operating construction disbursement and all other custodial accounts), including prohibition of commingling of accounts.
2. Require title insurers to provide a plain English disclosure which would notify insured of

exceptions within the title insurance policy. The disclosure should also notify home purchasers that a lender's policy protects the interests of the mortgage-lender, not the purchaser-mortgagor. If a purchaser decides to buy title insurance coverage, all fees or charges associated with obtaining the title insurance policy should be disclosed.

3. Require title insurers to conduct annual onsite reviews of underwriting, claims and escrow practices of title insurance agencies or agents with which they have contracts. Each title insurer should adopt standards and procedures to be used during the onsite reviews.
4. Require title insurance premium rates be sufficient to cover projected losses and expenses, allow for a reasonable profit, but should not be regulated to such a degree that such rates discourage competition or burden the consumer.
5. Require title insurers to issue closing or settlement protection letters to protect the buyer, lender, and seller's interest in the event of theft of settlement or escrow funds by the title agent or the title agent's failure to comply with closing instructions.
6. Require deadlines for policy issuance. Title insurance policies should be issued within 45 days of closing.
7. Require more professional licensing requirements for title insurance agencies and agents. The law should require employees of title agencies to be licensed or named on the title agent's license if the employees engage in functions of a title insurance agent. Title insurance agents should be required to complete 16 hours of continuing education courses related to title insurance every two years.
8. Require title insurers, title agencies or title agents to disclose affiliated business arrangements to their customers. If the transaction involves an affiliated business arrangement, a written estimate of the charges shall be provided to the customer.
9. Prohibit title insurers, title agencies, or title agents from giving or receiving consideration for the referral of title insurance business, including escrow, closing or other services provided by them.
10. Prohibit title insurers and title insurance agents from participating in transactions in which they know another party requires the purchase of a title insurance policy from a particular insurer or agent as a condition precedent to obtaining a loan or other services.

11. Prohibit title insurers or title insurance agents from offering payments, rebates or other inducements as part of a title insurance transaction.
12. Prohibit title insurers or title insurance agents from making payments or withdrawals from a settlement escrow account unless a corresponding deposit of funds.